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## HOW WILL CROP PRODUCERS AND CONGRESS RESPOND TO HIGHER PRICES?

Wheat, corn, and soybean prices have moved higher since mid-September. Higher prices have implications for the production plans of farmers and perhaps for farm policy.

December 2006 corn futures reached a contract high of \$3.17 on October 13, \$.81 above the mid-September low. The average spot cash price of corn in central Illinois increased from \$2.09 on September 12 to \$2.92 on October 13. The rally late last week reflected the USDA's October *Crop Production* report. The 2006 U.S. corn crop is forecast at 10.905 billion bushels, 209 million below the September forecast. The forecast reflects a yield of 153.5 bushels, 1.2 bushels below the September forecast, and harvested acreage of 71.047 million, 794,000 below the September forecast. With consumption of U.S. corn during the current marketing year forecast at 11.89 billion bushels, year-ending stocks are forecast at a meager 996 million bushels. The USDA projects the marketing year U.S. average farm price in a range of \$2.40 to \$2.80. At the close of trade on October 13, futures prices translated to a marketing year average farm price of about \$3.10 per bushel.

November 2006 soybean futures traded to \$5.945 on October 13, about \$.58 above the mid-September low. The average cash price of soybeans in central Illinois increased from \$5.045 on September 6 to \$5.615 on October 13. The USDA now projects the 2006 U.S. soybean crop at a record 3.189 billion bushels, 96 million larger than the September forecast. The U.S. average yield is forecast at 42.8 bushels, one bushel above the September forecast. Harvested acreage is forecast at a record 74.505 million, 570,000 more than projected in September. Even with consumption of U.S. soybeans forecast at a record 3.086 billion bushels, U.S. stocks are expected to grow from 449 million bushels on September 1, 2006 to 555 million on September 1, 2007. The USDA projects the marketing year average farm price in a range of \$4.90 to \$5.90. At the close of trade on October 13, the futures market projected an average farm price of about \$5.90.

December 2006 wheat futures at Chicago traded to a contract high of \$5.51 on October 12 and closed at \$5.255 on October 13, \$1.34 above the mid-September low. July 2007 futures settled at \$4.625, \$.40 above the mid-September low, but \$.255 below the contract high established on October 4, 2006. Old crop wheat prices are being driven by prospects for a 2006-07 world wheat crop that is 5.4 percent smaller than last year's crop and 4.8 percent less than projected consumption. Among the major wheat producers, only China

is expected to have a larger harvest than last year. The largest drop in production, 55 percent, is expected in Australia. World wheat stocks as a percentage of use is expected to decline to a record low level this year. The USDA projects the U.S. average farm price of all classes of wheat during the current marketing year in a range of \$4.10 to \$4.70. The record high average price was \$4.55 in 1995-96.

One of the questions generated by high prices is “How will U.S. and world producers respond?” In the U.S., available crop land is generally fully utilized so there is little opportunity to expand total acres planted. The expectation is that acreage devoted to wheat and corn will increase and that acreage of most other crops will decline in 2007, but the magnitude of change can still be influenced by changes in price levels, with the exception of winter wheat. The USDA will survey winter wheat producers in December and report planted acreage on January 12, 2007. At this juncture, a significant increase in acreage is expected. Current futures prices for the 2007 corn and soybean crops favor corn production over soybean production in parts of the corn belt. The prospect of ample U.S. and world soybean stocks in contrast to small corn stocks and rapidly growing corn consumption, suggests that corn acreage needs to increase at the expense of soybeans and other crops in 2007. It will be up to the market to give the appropriate signals, avoiding the mistake of a year ago when the market incorrectly signaled more soybean and fewer corn acres. On a world level, wheat acreage will likely expand in response to current high prices. If U.S. soybean acreage declines in 2007, prices may have to move to a level that will encourage more acres in South America a year from now.

A second question generated by current prospects for high prices is “How will Congress respond?” Projected prices are well above current support prices so that producers may receive only direct payments for the 2006 crops. The main issue is whether these higher prices are expected to persist. If so, Congress could respond by keeping commodity programs generally in tact in order to minimize budget exposure. Alternatively, Congress could view this as an opportunity to move the focus of policy away from price supports. A related issue is whether Congress will reduce or eliminate current domestic and trade policies that prevent the market from directing production and consumption decisions.

Issued by Darrel Good  
Extension Economist  
University of Illinois